The Province of Alberta

IN THE MATTER OF "THE NATURAL GAS UTILITIES ACT"

—and—

IN THE MATTER OF an Enquiry into Scheme to be adopted for Gathering, Processing and Transmission of Natural Gas in Turner Valley

G. M. BLACKSTOCK, Esq., K.C., *Chairman*

Dr. E. H. BOOMER, F.C.I.C., *Commissioner*

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10.00 A.M.Session,
March 12th, 1946.

MR. CHAMBERS: I will call Mr. McLellan.

G. R. McLELLAN, having been recalled, direct examination by Mr. Chambers continued:-

Q Mr. McLellan, you are still under oath?

A Yes.

Q You have prepared, as I understand it, a statement in respect of the operations of the Gasoline Department of Royalite Oil Company Limited for 1939 to 1948, the one from 1946 to 1948, of course, is estimated?

A From 1945.

Q From 1945.

MR. CHAMBERS: Now Sir, I have circulated copies of this to the others, and I had two for you this morning.

SUBMISSION PRODUCED HERE MARKED EXHIBIT 156.

Q MR. CHAMBERS: You might read the narrative part of your statement, Mr. McLellan, and make such comments or explanations as you wish to, as you go along, and also deal with the accounting?

A I start on Page 3 "Royalite Oil Company Limited, Gasoline Department."

This submission is a summary of the operations of the Gasoline Department of the Royalite Oil Company Limited, for the years ended December 31, 1939 to 1944 inclusive, together with estimated operating results for the years 1945 to 1948 inclusive. Also attached are subsidiary statements and schedules supporting actual and estimated operations of this

department.

The Statements and Schedules which are being submitted are listed with abbreviated descriptions on the index, being pages 1 and 2 of this submission.

The Statements and Schedules are discussed below under the following headings:

(1) Allocation of Indirect and Administrative Expenses.

(2) Calcaulation of Depreciation.

(3) Allocation of Gas Gathering and Compressing Costs.

(4) Calculation of Investment.

(5) Estimated Operating Results.

(6) General

(1) Allocation of Indirect and Administrative Expenses

In order to arrive at the operating costs of the Gasoline Department, it was necessary to distribute the items of expense which in the ordinary course of events are not distributed on the books of the Company. These expenses come under the following main Classifications:

Employees Welfare Expense

Administrative and General Expense

Profits and Losses on Service Units.

For the purposes of this submission, the first two classifications have been distributed on a direct labour basis to the main departments and also to the utility and service unit accounts. These items have then increased the losses or decreased the profits shown by such utilities and service units, and the resulting profits or losses have then been distributed to the main departments in the same proportions

as the original charges for such utilities or service units were made on the books of the company.

(2) Calculation of Depreciation

For the purposes of this submission, the unit method of depreciation,has been used for all assets with the exception of the Boiler Plant, Electric Plant and the North Return Fuel Line.

The depreciation on the Boiler and Electric Plants (included in the proportion of the operating costs of these plants charged to the operations of the Gasoline Plant #1) has been calculated on a straight line basis with the assumption that the two plants have a 30-year life from December 31, 1943. Operating Expenses of Gasoline Plant #1 shown on Schedule A, have been calculated using book depreciation with respect to Boiler and Electric Plants. Schedule "G" adjusts these operating expenses in order to reflect the revised depreciation calculation.

It is estimated that the North Return Fuel Line will have an estimated life of 40 months, being from March 1, 1944 to June 30, 1947. The estimated salvage value has been deducted from the cost of this line and the resulting amount has been spread over the 40-month period. This results in an amount of $1,055.33 per month being charged to the Gasoline Department Operations as depreciation in respect of the North Return Fuel Line.

(3) Allocation of Gas Gathering and Compressing Costs

Gas Gathering and Compressing costs of the North System, which comprises the North Gas Gathering Lines and the Compressor #1, have been allocated to the Gasoline Plant #1 and the Scrubbing Plants on a volume basis.

Q MR. CHAMBERS: My copy has on it there "All lines currently attributable to compressor No, 1."

A Yes, that is so. I have not got that on my copy.

Q All right?

A This gives the following percentages of Gas Gathering and Compressing Costs to be charged to the Gasoline Plant #1.

1939	4.99%
1940	6.18%
1941	6.79%
1942	6.40%
1943	7.78%

Gas gathering and compressing costs of the South System which comprises the South Gas Gathering Lines and the No. 3 and No. 2 Compressor Plants, have all been distributed to the No. 2 Gasoline Plant for the years 1939 to 1942 inclusive.

In 1943 the South System was used by the No. 2 Gasoline Plant for 10 months of the year and for the remaining 2 months by the North System. The distribution was made on this basis, with the No.2 Gasoline Plant being charged with 10/12 of the costs and the No. 1 Gasoline Plant with 7.78% of 2/12 of the costs.

That 7.78 is much higher than in 1943 in the list of percentages.

(4) Calculation of Investment

The investment has been calculated as at June 30 in each year. This is done by taking the difference between the asset and the reserve for depreciation at January 1 of the particular year and adding to or deducting from this total one-half of the additions to or deductions from the asset and one-

half of the additions to or deductions from the reserve for depreciation.

That is we just took a balance at January 1st, and divided each addition or deduction in half.

This is on the assumption that all additions or deductions are only in the investment for 6 months. This procedure is followed for each individual asset and for each year.

The Investment in Gathering and Compressing assets has been allocated on the same basis as the operating costs of these same assets were allocated.

The Boiler and Electric Plant Investments have been allocated in the following percentages to Gasoline Department; and there are two columns "Boiler Plant" and "Electric Plant", and I had better read the Boiler Plant straight down first, and then the Electric Plant.

	Boiler Plant	Electric Plant
1939	72.52%	29.79%
1940	55.00%	21.28%
1941	63.63%	24.05%
1942	28.66%	23.37%
1943	37 %	25.5 %

These percentages are the same as those used in allocating the expenses of these plants to the Gasoline Department.

(5) Estimated Future Operating Results (1945 to 1948 inclusive)

Revenues

These are calculated by using the estimated gas to be processed, which is shown in the

Madison Natural Gas Company Limited submission M-2 (revised) and I have not got the exact number of that if you want that.

Q MR. CHAMBERS: I think it is Exhibit 47, or Exhibit 48, I am not sure which.

THE CHAIRMAN: I don't remember either.

(Exhibit 47)

It is assumed that the present product will not be manufactured after the end of 1946. If such is the case, the number of barrels recovered from a certain amount of gas will be less than in the years 1945 and 1946. The estimated revenues for the years 1947 and 1948, have accordingly been reduced. The 1945 Revenues are the actual receipts shown by the books of the company.

Share to Producer

This has been estimated at 20% of the estimated revenues, with the exception of the year 1945, where the figures represent the actual amount of the payments made to the producer.

Expenses - Operating

These are estimates which were confirmed by the Superintendent of the Gasoline Department. The estimates for Steam and Electricity were taken from the Madison Natural Gas Company Limited, submission M-9, and the same answer there. (Exhibit 79).

Depreciation

This is based on an estimated throughput basis with the throughputs taken from the Madison Natural Gas Company Limited submission M-2 (revised) and the same thing there. (Exhibit 47).

Gas Gathering and Compressing Costs.

The portion applicable to the Gasoline Plant shrinkage has been taken from Madison Natural Gas Company Limited submission M-12D. The portion applicable to the gas passing through the North Return Fuel Line has been estimated in the same manner as that shown on the submission M-12D. (Exhibit 81)

(6) General

When reading any of the attached statements or schedules, all figures should be read as dollars and cents unless otherwise indicated.

Income Tax has been calculated at the following rates; and there is "Dominion", "Provincial" and "Total".

	Dominion	Provincial	Total
1939	15%	7%	22%
1940	30%	7%	37%
1941	40%	Nil	40%
1942	40%	Nil	40%
1943	40%	Nil	40%
1944	40%	Nil	40%

Details of Gas Processed and estimated to be processed in each of Gasoline Plant #1 and Gasoline Plant #2 are also attached hereto and form the last two pages of this submission.

Q MR. CHAMBERS: And now you might take us through the statements and schedules, Mr. McLellan, and draw attention to anything you have in mind?

A All right.

The first statement, Statement 1 is a statement showing the results of Gasoline Department operations for the

years ended December 31st, 1939 to 1944 inclusive, using the unit method of depreciation.

There is the profit of the #1 plant per statement 2, and the profit or loss of the Gasoline Plant #2, per Statement 3. Then income tax is deducted as stated on page 7, giving us the net profit after income tax and we show then the investment in plant and equipment, which is shown on Statement 5, and the percentage earnings on investment which those profits reflect in the earnings which have been made on the investment in the plant and equipment.

Also for information is the barrels produced in the Gasoline Plants 1 and 2.

Statement 1(a) is of the same nature except that the figures are estimated. There are the revenues and then operating expenses and then depreciation and then the gas gathering compression costs.

There might be some doubt about that, because the gas gathering compression costs there, it is the amount, probably you should put in "attributable to gasoline plant #1 and attributable to North Return Fuel Line."

And that statement is calculated very similar to the first one.

Statement 2.....

Q MR. BLANCHARD: Excuse me, are these compression costs related to the North Return Line shown on any separate schedule?

A No, they are not.

Q They are combined with gathering costs?

A They are just calculated in the same manner as the gathering and compression costs, attributable to the Gasoline Plant #1, which is taken from M-12-D and on M-12-D there was no calculation of this nature made for the North Fuel Line, so I

have done one similar to that.

Statement 2 shows the details of the operations of the Gasoline Plant #1. Statement 3 shows the details of the Gasoline Plant #2. Statement 4 is a statement of Gas Gathering and Compressing costs for the years ended December 31st, 1939 to 1943 inclusive, using unit method of depreciation.

Now that is divided into two systems, the North system and the South system, and the expenses of each unit are shown separately.

In 1943, as I stated in the report, the South System was used for only ten months by the Gasoline Plant #2, so the allocations made at the bottom of the page under "1943" were the amounts applicable to the North System, going up and being shown as the last item under 1943, that is $9,107.93.

Q MR. STEER: I just cannot follow you there, Mr. McLellan, are you talking there about Statement 4?

A Statement 4, yes.

Q Would you mind repeating what you said about it?

A With regard to the breakdown of the 1943 costs of the South System?

Q Yes?

A The South System in 1943 was used only ten months by the Gasoline Plant #2.

Q Oh yes, I see.

A And so we have to make an allocation of those ten months to the South System and two months to the North System.

Now the amount applicable to the North System shows at the bottom there, $9,107.43. That then was taken up and shown as the last item under the North System in 1943. The percentages shown there, being the distribution or the allocation of the North System between the two, the Gasoline Plant #1,

where the same percentages which I mentioned in the report earlier, and they are calculated on the volumetric basis. Statement 5 shows the total investment....

Q MR. CHAMBERS: Mr. McLellan, would you go a little more slowly at this, just take your time?

A Yes. Statement 5 shows the total investment in, for the years 1939 to 1944 inclusive, the total investment in the Gasoline Department. Those were calculated as at June 30th in each year.

We have the Gasoline Plant #1, which is the actual investment in the plant proper, firstly. Then we have the Electric Plant and Boiler Plant, just a share.

Now that was done that way to keep the investment in each of those plants separately, and then taking the proportion of that investment and allocating it to the Gasoline Plant Department. The proportion is the same proportion as mentioned earlier in the report and is the same proportion of the Gasoline Plant, the Electric Plant and the Boiler Plant, the assets, and it was done in the same manner as I show, as a division of the operating expenses of those two plants.

Now the North Gas gathering and compressing unit, that was done in the same manner. We calculated the investment and then we allocated the same proportion to this account as we had the operating expenses of those plants.

The working capital shows "cash" and "inventory". The cash is 1/8 of those out-of-pocket expenses. That is simply the out-of-pocket expenses divided by eight, and the inventory, $20,000.00 is the same in all years. I got an actual inventory from our field superintendent for that figure. He gave me that figure and for the estimated, that is from 1945 on, and for lack of a better figure I have used the same one

as in the past years.

North Return Fuel Line is all allocated to the Gasoline Plant, as it is the only plant which it serves.

Gasoline Plant #2, the Gasoline Plant #2 and Refractionator, the Refractionator is part of the Gasoline Plant #2. That is all allocated 100%.

The South Gas Gathering and Compressing units are just a share of that. I say "share" there because in the year 1943 there was a division. In all other years it was 100%.

Working capital account is 1/8 of the out-of-pocket expenses for cash, and I have taken no inventory on the basis that the inventory for the #1 Plant would be sufficient to serve in the Number 2 plant as well.

The total for the #1 Plant investment in the case of 1939 is $412,171.10. In the case of the #2 plant, $534,055.20, giving a grand total of $946,226.30.

And the other years, of course, go accordingly.

It will be noted in the year 1944, the Electric Plant, the Boiler Plant and the Gasoline Gathering and Compressing Units do not show, the reason for this being that the assets have been, were transferred to the Madison Natural Gas Company Limited, and they are no longer in the investment of the Royalite Oil Company.

(Go to page 5873)

Statement 6 is calculated in the same manner as Statement 5 with the exception that the assets which are now owned by the Madison Natural Gas Company Limited are not of course included.

Schedule "A" is a detailed analysis of the operating expenses excluding depreciation for the years 1939 to 1944 inclusive of the gasoline plant No. 1 proper. They just come under the ordinary headings of administration and general expense shown at the bottom.

Schedule "B" is the operating expense of gasoline plant No. 2 in the same manner as gasoline plant No. 1. I do not think there are any particular items in there that would cause comment.

Schedule "C" is the same thing for the gas gathering lines north.

Schedule "D" for gas gathering lines south.

Schedule "E" for the compressor No. 1, and Schedule "F" for the compressor No. 3. Schedule "G" was necessitated because of the change in calculation of depreciation on the boiler plant and electric plant.

Schedule "A" which is the operating expense of gasoline plant No. 1 is calculated using book depreciation for the boiler plant and electric plant. By changing the depreciation in these two plants of course the expense chargeable to gasoline plant No. 1 has also to be changed and this statement makes the necessary adjustments.

Schedule "H" is a statement of the changes in fixed assets and the relative reserves for depreciation of the gasoline plant No. 1 from January 1st, 1939 to December 31st, 1948 and using the unit method of depreciation with

estimated throughputs for the years 1945 to 1948 inclusive. That just shows the balance at the beginning of the period, additions, deductions and any other deductions. Other deductions might possibly be explained. In the course of changing these plants over, that is transferring gasoline plant No. 2 to gasoline plant No. 1 there were certain transfers of assets back and forth and new additions, out of pocket expenses, and all these were for convenience. I mean it does not add anything to the statement really, just more for our own convenience we put those under other deductions and additions and the reserves for depreciation are calculated in the same way. The provisions for one year are calculated, of course, on the unit method of depreciation, and the next column "Depreciation transferred, less depreciation restored, due to sales, retirements" includes both depreciations which have come over from one asset to another asset and from that is deducted any depreciation which of necessity is restored when sales or retirements are made. Then of course we come to the balance at the end of the last period.

Schedule "J" is the same details with regard to gasoline plant No. 2. You will notice in 1943 there are two items, for 1943, one ending on October 31st, 1943. The item $372,495.14 is the balance remaining when this plant was closed down and depreciation has been calculated only up to that point. The next item under date 1943 shows a blank and the reason for that is that this depreciation was calculated only up to January 1st, 1943. That is about all there is on that one.

Schedule "K" is the boiler plant and electric plant which I think we have discussed in some detail.

This is not calculated on the unit method but on the straight line method, using 30 year life from December 31st, 1943. For an example of that we might take an asset which was acquired in 1938. The period at which this asset will then be in use is calculated as 35½ years. Now that is calculated by taking the year 1943 from which the 30 year life is based, subtracting 38 it gives it a 5 years and we add one half year assuming the asset was acquired in the middle of 1938 and giving us 5½ years, plus the 30 already mentioned gives us the 35½ years. At the end of 1943 the asset then has been depreciated 5½, thirty-five and halves.

Schedule "L" is the details of the gas gathering lines north together with gas gathering lines south and is calculated in the same way, that is gasoline plant No. 1 and gasoline plant No. 2. That is on the unit method of depreciation.

Schedule "M" is compressor No. 1 and compressor No. 3 also on the unit method.

Schedule "N" is compressor No. 2 and that is also calculated on the unit method.

Schedule 1, are the estimated operating expenses excluding depreciation for the years ending December 31st, 1945 to 1948 inclusive. Now these are estimates which were confirmed by our Superintendent in Turner Valley with the exception of the calculations of steam and electricity which were calculated from the Madison Natural Gas Company's submission M-9. Welfare expense is estimated as 18% of labour. That is the same proportion as 1944 expenses are worked out. Included in Schedule 1 is the figure for district expense. For schedule 2, Schedule 2 shows the details of this

district expense which is estimated will be chargeable to the gasoline plant. I do not think there is anything particular in that that will cause any comment.

MR. HARVIE: I wonder if you would be good enough to explain how you arrive at this 87½% of share of gasoline plant No. 1 in Schedule 2.

A This district expense is what we call expense of certain office personnel and Superintendent of the plant and those people spend approximately 87½% of their time on the gasoline plant No. 1 and some of it they spend on the water system and various other small parts of the organization, so that only 87½% of their expenses are chargeable to the gasoline plant. That is an estimated figure for the years 1945 to 1948.

Schedule 3 is the estimated operating cost of the north return fuel line for the years 1945 to 1947 inclusive. That just goes to the year 1947 because it is estimated that the north return fuel line will be all through at June 30th, 1947.

Schedule 4 shows the details of the assets and calculation of depreciation. The total cost is $75,584.55. There is an estimated salvage of $33,371.43, giving a net of $42,213.12 and as there are 40 months this amount is divided by 40, giving us $1,055.33 per month to be charged to the operations as depreciation. Now that depreciates this asset down to the salvage value.

Q MR. CHAMBERS: That line is on top of the ground as I understand it ?

A This line is on top of the ground, yes. The last two pages gives the details of throughputs, estimated throughputs. Firstly in gasoline plant No. 1 and they are expressed in thousands of

cubic feet. The actual and estimated throughput to December 31st, 1948 is 323,651,370 thousand cubic feet. From January 1st, 1949 to December 31st, 1974 the estimated throughput as per the Madison M-2 Revised shows 290,678,000 thousand cubic feet. Giving a total reserve of 614,329,370 thousand cubic feet. The No. 2 is just the actual throughputs from the commencement of operations to the end of 1943.

Q It has just occurred to me Mr. McLellan, that you must have had some estimate of your revenue ?

A Estimated revenue, yes I did.

Q For the future ?

A Yes.

Q And that would be based on so much gasoline manufactured ?

A So much gas processed.

Q And that ends up with so much wet gas to sell from which you would get revenue ?

A That is right.

Q Have you got that available ?

A No, I have not those figures with me. On Page 6 of the report here I think I mentioned the way of calculating that. These are calculated by using the estimated gas to be processed which is shown in the Madison Natural Gas Company Limited submission M-2 Revised.

Q Now will you turn to Statement 2 for a moment. The last item prior to the totals. Profits of gasoline plant No. 1 paid under compensation scheme settlement shown in 1943, $96,696.59. Now am I right in this that that is only part of the total amount that was paid under that compensation settlement ?

A That is right.

Q Do you know offhand what the total was or roughly ?

A I know exactly, $196,584.31.

Q And of that total amount that sum of $96,696.59 is shown charged to this operation ?

A That is right, to the gasoline plant operation.

Q Now I think you were present the other day when some discussion and evidence concerning Exhibit 147 which is commonly known as the A.W.S.C. contract ?

A Yes.

Q Now my understanding is that under the A.W.S.C. contract the Royalite Oil Company Limited did receive from the Allied War Supply Corporation on behalf of His Majesty one of the parties mentioned in Exhibit 147, a sum of money in respect of installations and changes made by Royalite in its absorption plant ?

A Yes.

Q Now can you tell us what that amount was ?

A Well it was received in two amounts $95,400.00.

Q $95,000.00.

A $95,400.00 and an additional amount of $13,595.12, making a total of $108,995.12.

Q When did they get this amount back in 1943 ?

A The $95,400.00 was received December 18th, 1943 and the $13,595.12 on April 17th, 1945.

Q Now would you tell us where, if at all, that amount or any portion of it is shown in this statement that you have prepared Exhibit 156 ?

A Those figures do not appear anywhere in this statement.

Q And would you -

A The reason for that -

Q Yes.

A The reason for that is that I forget the clause in that contract. However there is a clause in the contract with the Allied War Supply Corporation which states that this amount is subject to revision. That is, there is a certain way of calculating the peace time value of this plant and when such calculation has been made then either the Royalite Oil Company will refund a certain amount of this money to the A. W. S. C. or else receive some more money. Now it has not been settled yet and we might possibly have to refund the whole amount. I have not taken it into my calculations at all as I do not know how much of it to take or how much not to take.

Q And would you turn to Schedule "J" I think it is. This is a statement about gasoline plant No. 2.

MR. HARVIE: What Schedule Mr. Chambers ?

MR. CHAMBERS: Schedule "J".

Q MR. CHAMBERS: And I notice from the end of 1945 down to the end of 1948 in the first column and also in the fourth column the amounts there are shown as constant. The same amount each year. Would you please comment on that ?

A Yes. That $205,827.76 represents the book value of these assets which remained in gasoline plant No. 2 after the transfer from this plant to the No. 1 plant. That is, it was closed down on October 1st, 1943 and certain of the equipment was transferred up to the No. 1 plant and there still remains certain equipment which is still at the location of the gasoline plant No. 2. Now when you are considering this $205,000 you should also consider the amount of depreciation which has been accrued against that. That would be against the $205,000 we would have $61,524.47 which is found in the last column against the year 1945.

Q So that, as I understand it, Schedule "J" in effect means that as from the end of '45 on, although the No. 2 plant is not operating and has been closed down, Royalite had certain assets that had not been fully depreciated to the extent of $205,827.76 less $61,000.00?

A That is right.

Q $61,524.47?

A Yes.

Q And that that amount is reflected in your costs?

A Yes. We have this continued depreciation on those assets which is as if they were still, which is as if the plant were still being operated on the theory that this money was invested in the Gasoline Plant Department, and we have expected to recover the whole thing.

Q Yes?

A So that this loss is being spread over the future operations of the Department?

Q Now, would you turn to Statement 1, please, Mr. McLellan. Turn to where you show the percentage of earning on investment for each of the years 1939 to 1945?

A Yes.

Q Have you by any chance the average of those?

A Yes, Statement 1 itself, it shows the average earning is 10.49%.

Q Where is the other?

A It is the next one.

Q Yes, the next one. It is '45 to '48 inclusive?

A '45 to '48 inclusive, the average for those four years is 5.33%.

Q Yes?

A And then if you take the whole ten years together, we get

an average return of 8.84%.

Q And that is after income tax?

A Yes, that is after income tax.

Q After it is calculated?

A Yes.

Q MR.HARVIE: Would you give me that first percentage again?

A For Statement 1?

Q Yes?

A 10.49%.

Q MR.McDONALD: And for ten years?

A Beg your pardon?

Q That last figure, the ten year figure?

A 8.84.

Q MR. CHAMBERS: That is all, Mr. McLellan. Answer my learned friends.

THE CHAirman: Mr. McDonald?

MR. McDONALD: I have not anything just now, Sir.

THE CHAIRMAN: Pardon?

MR. McDONALD: I have not anything just now.

THE CHAIRMAN: Mr.Steer?

MR. STEER: I presume,Sir, that Mr. Hamilton is going to examine this statement and perhaps have access to the Company's records, so that he will be able to verify it?

THE CHAIRMAN: Yes. He has that statement now, I believe.

MR. CHAMBERS: Yes, it was sent to him Wednesday of last week, I think.

THE CHAIRMAN: Yes. He could not be here today, although I understand he has been doing some work on it. Mr. Hamilton wanted some information. Has he called on you for

any information, Mr. Chambers?

MR. CHAMBERS: Yes. As a matter of fact, I think Mr. McLellan dealt with most of that this morning.

THE CHAIRMAN: Yes, I see.

MR. CHAMBERS: Mr. Hamilton did indicate that he did not intend to go through the books, but he probably has something in mind. He has been given that statement anyway, and Mr. Hamilton did make an examination of one year, wasn't it, Mr. McLellan?

THE WITNESS: Yes, the year 1943.

.....

CROSS-EXAMINATION BY MR. STEER.

Q Would this be true, broadly speaking, Mr. McLellan, that these statements are prepared by you going back over the years mentioned through the books of the Royalite Company and re-writing those books for these purposes?

A Practically, yes.

Q And I suppose the re-writing of them was necessitated largely by the fact that you have used the unit method of depreciation, was it, throughout?

A Well that would be one part of it. The main job was the distribution of the administrative and indirect expenses, and the welfare expenses.

Q Administrative and what?

A Administrative and Indirect.

Q And Welfare?

A Yes, and Welfare.

Q In the Royalite books are direct operating expenses charged directly to the various departments?

A Well,.....

Q Have they been throughout the period?

A Not to the various departments, no.

Q Well then.....

A We have what we call main classifications of accounts, but not department.

Q I see. Then wouldn't you have to distribute all labour costs as well as indirect costs?

A All labour costs?

Q Yes?

A What do you mean by that?

Q There are three departments to this business, as I understand it. There is the crude oil department, the gasoline department, and the gas department, is that right?

A Well, we have not got the gas department now. We had at that time.

Q I am talking now about the period prior to the 1st of January, 1944?

A That is right.

Q Now do I understand you to say that your costs, what I may call your direct costs of those various departments, were not charged directly to those departments?

A That is right.

Q That is right?

A Yes.

Q Then when you are restating these figures, it would be necessary for you to allocate these direct costs as well as your indirect ahd administrative costs, is that right?

A That is right.

Q And the service costs?

A And the service costs. I include those in indirect.

Q You include which?

A The profits or losses on service units I included in indirect.

Q Yes. Are we to take it then that your indirect administrative and service costs were allocated to these three departments on the basis of the labour costs involved in each one of the departments?

A Not exactly, no. The labour costs, I assume you mean welfare expense, etc.?

Q No, I mean direct labour, the labour that goes into the Department?

A The direct labour was charged to the main classifications, as I say. That had already been done. I did not have to charge that.

Q That is what I was trying to get at a minute ago, and you told me, I think, that.....

A There is just one point though there. For instance, our gas gathering and compressing costs, they have to be allocated. They are carried on our accounts as gas gathering and compressing costs, and they have to be allocated to the Department.

Q That is so. I asked you whether or not direct costs of the three departments had been kept track of in the company's books. Now, what is your answer to that? You know what I mean by direct costs?

A They have been kept track of but not as departments.

Q Very well then. If those direct costs have not been charged to crude oil, gasoline and gas, then it must have been necessary for you in preparing this statement to make an allocation of that to those three departments?

A It was.

Q Yes? So that you have had to go back to the books and re-write those books with respect to the direct costs as well as indirect costs?

A The direct costs only in the gasgathering and compressing costs.

Q Of course, gas gathering and compressing costs were always attributable both to the gasoline and the gas departments, weren't they?

A Yes.

Q Yes. So that they would come, or I would suggest to you that they would come at all times under what we might call direct expenses?

A Oh not necessarily. I do not think they are direct expenses.

Q Is there any difference between these gathering and compressing costs and general overhead?

A I think there is.

Q What is the difference?

A Well, they are direct and can be directly chargeable to one particular unit.

Q What about the compressing and the gathering?

A No. The actual costs, those can be charged against the compressing unit, whereas your actual general overhead costs cannot be specifically allocated to any one department.

Q Well, I suggest to you that the only differencee between your overhead and your gathering and compressing is that your overhead is charged among three departments and your compressing and gathering are charged among two.

A Well, they are charged in that manner, yes.

Q Now, can you go to the books of the Royalite Company Limited as they are written and tell me the direct labour costs of the Gasoline Department?

A Yes, I can.

Q As they are written?

A Not the Gasoline Department. I can tell you the gasoline plants.

Q You can tell me the labour charges, the moneys that were expended for labour for men who were employed at #1, and #2 Gasoline Plants, is that it?

A Direct labour, yes.

Q The direct labour?

A Yes.

Q That labour, of course, would have, however, to be divided for the purpose of this statement of yours, general, gasoline and gas, wouldn't it?

A Not if the men worked in the two gasoline plants.

Q Pardon?

A Not if the men worked in the #1 and the #2 gasoline plant as you said.

Q Then, do you say that your gasoline operations are an entirely separate operation from your gas operation?

A I say the costs can be divided.

Q And are not divided on the books at the present time?

A That is right.

Q And you have had to divide them for the purposes of these figures?

A Yes sir.

Q On what basis did you divide them?

A I divided the gas gathering and the compressing costs of Gasoline Plant #1 and the gas gathering and compressing costs of the North System on the volumetric basis.

Q Yes?

A And the gas gathering and the compressing costs of the South System were entirely charged to the Gasoline Department with the exception of the year 1943, when they were divided.

Q Yes. Apart from those gathering and compressing costs, are there any costs which are common to gasoline and gas?

A There is the Electric Plant and the Boiler Plant expenses, which are divided between the gasoline business and the gas business, and the crude oil department as well.

Q Any others?

A Well, the majority of our service units are allocated between one and another.

Q What do you mean by service units?

A Well for instance, our expense of our forge and the machine shop are divided between the gasoline plant and the gas business, and again, the crude oil department, the whole three.

Q Yes? And anything else?

A I think those are the direct items. I mean, when I say forge and machine shop and service units, I mean all of our various services which we have in the field.

Q Perhaps we can shorten it if I suggest to you that the books of the Royalite Company have not been kept strictly by departments, that is to say, charging up labour that you know to have been expended in a certain department. You have not even done that?

A It has been done to a certain extent.

Q To what extent?

A Well, when I say to a certain extent, I say it has not all been done, and I mean certain of these have been done.

Q Then it follows that no one can go to those books and find out what direct labour has been charged to any particular department if it has not all been done?

A Directly it has been charged to the individual units, but not to individual departments.

Q I see. I am talking about departments now. What was transferred from the Royalite Company to the Madison Company was your Gas Department, is that right?

A Yes.

Q Can you go to the books of the Royalite Company and tell me what the operating expenses were over the period '39 to '44 of that Gas Department?

A I can do it in the same manner as I have done the costs of this Department.

Q Of course, what I am getting at, Mr. McLellan, is how you have done this. Now, I suggest to you that you cannot even get direct labour of the Gasoline Department out of the books at the present time as they are written?

A I think I can get direct labour after we make this allocation to gas gathering and compressing costs.

Q Yes?

A And I am wondering if those direct labour charges, gas gathering and compressing costs, might be a service which is rendered to both Departments.

Q Yes?

A So that in that case we can give you the direct labour in that department.

Q I see. So that what I am getting at is, whether you found it necessary to make any allocation of the labour costs in this Gasoline Department for the purpose of arriving at your figures?

A The direct labour, I think I would say no.

Q So that you have got your figures here with regard to your direct labour directly out of the books of this company, is that right?

A That is right.

Q That is right?

A Yes.

Q And the only allocation that you have found it necessary to make was with regard to compressing and gathering costs?

A That is right.

Q And the same would be true of the Gas Department, would it?

A I would not like to say without looking into that.

Q Well, if it is true of the Gasoline Department, and the Gasoline and the Gas Departments are as intimately connected as they were, why wouldn't it be necessarily true of the Gas Department?

A Well, offhand I would say probably that it would, but I would not like to say definitely.

Q Yes, I see. Well then, your evidence now is that we can go to the books of the Royalite Company and we can find direct expenses applicable to each of the three departments?

A Yes.

Q Yes. And that the only necessity there has been for allocation is by reason of the fact that the gathering system and the compressing system serve both the Gasoline and Gas Departments?

A Yes.

Q And there is no common service performed by any parts of the Royalite undertaking for all three departments of the business, including the crude oil? The crude oil is something apart, is it?

A No, I say our service units can be divided between the three of them.

(Go to page 5890)

Q. I see, and your general administrative and overhead has got to be divided ?

A Yes, and the welfare expense.

Q What you say is you have taken that general administrative overhead and welfare expense of service units and you have divided them amongst these three departments on the basis of direct labour ?

A Yes.

Q And the direct labour you get actually out of the books of the Company ?

A Yes.

Q Will you tell us what the direct labour was, what the cost of the direct labour was for the gasoline, gas and crude oil departments of the Company for the year 1939 ?

A As I say I cannot give you that by departments. I can give you the direct labour in the department but there is also other labour that is charged to service units and to other expense accounts which themselves are allocated to those departments. So that you cannot take the total payroll and divide it so much to the gas department and so much to the gasoline department and so much to the crude department. You have to approach it on the overall cost of the unit and then distribute your units.

Q What you are saying in your report is you have taken these two things, you have taken the employees welfare expense and administrative and general expense and the profit and loss on service units and you have divided them up on the basis of the direct labour. I would like to know how you divided that, what figures you used ?

A We should go a little further, they have been distributed on

the direct labour basis to the main department and also charged to service units accounts.

Q They have been distributed to the main department, that is the crude oil, gasoline and gas ?

A A portion of them.

Q I would like to ask you, Mr. McLellan, if you will produce your figures, the figures on which you have made this computation and then we can perhaps understand it. I am bound to say that I do not understand what you have done ?

A Probably if I start at the first. Firstly, I get our direct labour in each unit, not the Department.

Q And by unit you mean - -

A For instance, gas gathering north and gas gathering south and forge and machine shop, boiler plant, electric light. Direct labour in the gasoline plant 1, and direct labour in gasoline plant 2, and all those various classifications. Then we take the employees welfare expense and administrative and general expense, firstly, and then we distribute those all over those various units. Then when we put this extra charge into our service units we increase the expense of those service units. Now then those same service units are then distributed back to the main department in the manner in which they were firstly distributed on the books of the Company. And then when we get them all charged back into the main department the cost of the service units those are closed out and there is no balance left in those. They are all distributed.

Q I guess that is clear to an accountant. My friend Mr. Smith says he understands it.

A He says he does - -

Q I would like to ask you Mr. McLellan with reference to

depreciation a question or two. Primarily this statement Exhibit 156.

A 156.

Q Was prepared to guide the Board in its allocation of proceeds of the sale of gasoline, as between the absorption plant and the producers ?

A Yes.

Q And you have adopted throughout the unit method of depreciation?

A Except for the things that you have mentioned.

Q Yes ? I am wondering whether for that purpose and for the purpose of showing the profits that have been earned up to date and the profits that are going to be earned in the future on your estimates, I am wondering if what you should not have done was to use the book depreciation of the Company ?

MR. CHAMBERS: I do not want to object for the reason of objecting but I do submit that an allocation as to the portion of the gasoline sales realization as between the absorption plant and the producers is none of the business - and I say this in no disrespectful way of my learned friend - that if there is any objection that lies in the mouth of Mr. McDonald, I do not want to be too technical on the thing but I do think we should each keep more or less in our own spheres.

THE CHAIRMAN: Supposing I asked the same question, Mr. Chambers.

MR. CHAMBERS: I do not think I could very well object to your asking it.

THE CHAIRMAN: I am going to ask Mr. Steer to ask it for me.

MR. STEER: I think perhaps, sir, we might as well get this question settled right now because I want to know whether

I am interested in this question of the division of profits of the sale of the gasoline to a producer in the absorption plant in any other capacity other than as a spectator. Because I am bound to say to my learned friend that I am going to be here as a spectator. My submission is I am interested in that and I am interested in seeing that the producer gets what is a fair and reasonable proportion of this gasoline content because the more he gets for his gasoline content the less in my submission he should get for his gas.

MR. CHAMBERS: By the same token the man that sells oil well equipment is interested probably because the well owner will then be able to buy more machinery and do more drilling.

THE CHAIRMAN: Well to the extent that the price of gas is affected, if it is affected by the gasoline content, to that extent Mr. Steer is interested. Now I think it will defy the Lord Chancellor to divide or to find the dividing line where his interest ends in this enquiry.

MR. CHAMBERS: Of course then I have one and I say fundamental objection to all of the evidence as to past profits or past losses or future profits or future losses so far as the prices to be fixed by this Board are concerned. I submit if we are going to fix prices on the basis of profits and losses or how much money the consumer or the party giving the service can pay from his earnings, well then I submit and I am taking this seriously and I intend to argue it seriously when the time comes for the final argument, if we are going to do that with one then everything all the way through should be treated that way.

THE CHAIRMAN: Mr. Chambers, probably I will put it this way. You know that the late W. S. Gilbert was a member of the

English Bar. He was also writing an opera. He was not on the practising list of Barristers. He was subpoenad to appear for Jury service on the morning on which he was producing his opera. He promptly paid his Bar fees and received a brief in the very trial in which he was subpoenaed as a Jurist. He did not appear but he was briefed. Now perhaps Mr. Steer is asking the question that Mr. McDonald wants to ask.

MR. CHAMBERS: Then I would like Mr. McDonald to say so then.

THE CHAIRMAN: Did you get the little analogy ?

MR. CHAMBERS: I would like to know if Mr. McDonald agrees to the position taken by Mr. Steer.

MR. McDONALD: No.

THE CHAIRMAN: Not to the extent that it will affect the wellhead price of gas.

MR. McDONALD: I am quite content to ask my own questions.

THE CHAIRMAN: Well I am not going to stop Mr. Steer yet in any event.

MR. McDONALD: Probably it might be quite in order to read the question that he asked. It slipped my mind what it was.

MR. STEER: I asked him whether in computing past profits and estimating future profits the Royalite Company for the purpose for which this statement has been prepared the book depreciation should not have been used instead of the unit method ?

A Am I to answer that one ?

MR. HARVIE: May I just say I should think, Mr. Chairman, this is probably bringing up the point I mentioned before. I

think possibly we were given the assurance by you that if this phase of the enquiry was put in at this stage that care would be taken to see that only those affected would be allowed to take part.

THE CHAIRMAN: That is right. Will you just define for me where Mr. Steer or Mr. Fenerty for that matter are excluded under that ruling, at the moment ?

MR. HARVIE: I will try to, yes. I think possibly there is a division as between all parties that are interested in the utility as such, the utility operations, that are interested in seeing what absorption operation pays or the gasoline plant operation pays for the services it receives. Up to that point I think there might be clearly an interest. Beyond that as to what division is made between the gross income or the net income, as might be decided, of the gasoline operations, as between the gasoline operator and the producer I do not think the outsiders have any interest in it. I think if they are now asking questionsas to how that division is to be made, as was intimated by my learned friend Mr. Steer when he said that he is interested in seeing how much the producer gets for his gas so that something else could be lowered, I think it is clearly not relevant in this part of the enquiry.

THE CHAIRMAN: Supposing I said I am going to take a broad general view of the whole picture to enable me to arrive at all just and reasonable prices that I have to fix.

MR. HARVIE: Yes. If that is the case I agree with Mr. Chambers, why pick out the absorption plant any more than any other user of the gas. Why not go to the drilling companies that are buying it. Why not go to the consumers in Turner Valley buying directly from the plant or the Alkylate plant

and all those things. I do object to having the absorption plant operation picked out and pulled to pieces on this basis unless it is going to be done all along the line.

MR. CHAMBERS: I would like to get the issue cleared up. Do I understand my learned friend to say that how much a well owner receives at the wellhead for his residue gas - -

MR. STEER: For his gasoline.

THE CHAIRMAN: What Mr. Steer said was this that he was interested in seeing that the producer got the largest possible share of the natural gasoline products so that he, Mr. Steer, could argue that he should receive less for the gas at the wellhead.

MR. CHAMBERS: That is the point I am getting at, maybe putting it the other way. How much the well owner receives for his residue gas at the wellhead has a bearing on the percentage of the division of the sale of gasoline. Or put it the other way, how much he gets from the gasoline is relevant in fixing the wellhead price of the residue gas. I think that is in effect what he is asking the Board to rule on as being relevant.

THE CHAIRMAN: And how much he gets for his crude oil.

MR. CHAMBERS: This is the first time the issue has been raised and it will be an important issue if it is persisted in.

THE CHAIRMAN: Mr. Chambers, surely Counsel have a right to argue along these lines if they wish to do so.

MR. CHAMBERS: He is asking you, as I understand it, to say that on that ground this evidence is relevant.

THE CHAIRMAN: No.

MR. CHAMBERS: If that is the case I would like a ruling one way or the other.

THE CHAIRMAN: What I have said, Mr. Chambers, is at the moment I think Mr. Steer is entitled to participate in this enquiry to the extent that the price of gas might be affected thereby. I do not know where the dividing line is. I am not going to attempt to draw it.

MR. CHAMBERS: He is leading this evidence as being relevant evidence. I mean otherwise he is not entitled to ask the question if it is not relevant. This opens up a large field.

THE CHAIRMAN: Mr. Steer can cross-examine on anything - -

MR. CHAMBERS: But I submit it must be relevant.

THE CHAIRMAN: If he is cross-examining on something the witness said surely that is relevant. It must be relevant. Your question is "What right has Mr. Steer to ask it?" It is not a question of relevancy.

MRE CHAMBERS: The information he is asking for must be relevant to the hearing. While I am registering my objection -

MR. FENERTY: May I put in a word. Probably there will be no objection. to me appearing because in this particular cross-examination as far as I now know I will not be taking any part but I certainly want to be here listening and having the opportunity of taking part if I so desire. My suggestion is this, apart altogether from the reasons advanced by Mr. Steer, that the only basis that any of our friends can say we are not interested in this enquiry is on the basis that we are not called upon to share any of the gathering costs. If, as I think is the case, and as I propose to argue now, apparently the absorption plant is not necessary and that we should take our costs from the down stream side of the absorption plant instead of the bottom of the well. If my learned friends

will agree with such a proposition as far as I am concerned I will fold up my books and go home. But just as long as there is any suggestion that the rate of return on this absorption plant or they propose to argue that that has any bearing on the division of costs, as long as there is any question of the division of those costs which I say are common, then I say we are vitally interested in what the proper depreciation should have been and how it should have been charged and what the future rate of return would be.

THE CHAIRMAN: This is what I have said, I think you are entitled to participate to the extent that it affects the price of gas. Where that point is I do not know. Do you object, Mr. McDonald, to Mr. Steer's cross-examination ?

MR. McDONALD: No, I do not object to Mr. Steer's cross-examination if he stays within the limits of his interests. The reason Mr. McLellan is in the box today and why you will have evidence next week as I understand it is this, that in this case or enquiry the question of the allocation of costs as between the absorption plant and the dry gas market has been mooted, first presented by Royalite and secondly by British American. They presented the volumetric basis of division. Mr. Steer made application to the Board that Mr. Mercer provide certain evidence in regard to the operation of the absorption plant for the purpose only of allocating those costs.

THE CHAIRMAN: Mr. Steer, Mr. McDonald ?

MR. STEER: Yes.

THE CHAIRMAN: It was Mr. Fenerty was it not ?

MR. McDONALD: It might have been Mr. Fenerty.

THE CHAIRMAN: He asked for the production of the Royalite

books in order that the allocation of those costs might be determined.

MR. McDONALD: Yes, and it was in answer to that application on which the Board ruled the evidence should be given, that we have this submission today. Now the Royalite Company have coupled with that submission a submission of the future operations of the absorption plant. This might not have been necessary for the purpose for which Mr. Fenerty's application was made. But we finally get down to the question I think the interest of the Gas Company and the City is simply on this matter of allocation and if they are going to propose that that application should be on the basis of the gross realization, that is the gross value of the gas and the gasoline that is one thing. All you have to know for that is what is the value now as divided between the producer and the absorption plant of the product which is not regulated and cannot be regulated by this Board. It is certainly of no interest to the Gas Company. It is beyond the Board's jurisdiction, and if the Board attempted to regulate it on that basis it would just mean that the producers, the price of gas would go up and down with the price of gasoline and all other things that enter into it. Some witnesses have referred to those difficulties.

(Go to Page 5900)

THE CHAIRMAN: I have to say that I have said something. However I will not say it again.

MR. FENERTY: My friend is thinking of beware of Greeks bearing gifts but I thought we might get together on a point.

MR. CHAMBERS: What is your proposition, fixing down stream the absorption plant.

MR. FENERTY: What I say at the moment -

THE CHAIRMAN: What he says is that the natural gas should bear no cost of the gathering behind the outlet of the scrubbing plant. We will come to that some day.

MR. CHAMBERS: The only remark I would like to make is that the absorption plant might not be there then. It might be somewhere else.

MR. McDONALD: I might suggest that the question asked Mr. McLellan was as to his opinion as to whether it should be done this way or not and I do not know that he is qualified to express an opinion one way or the other.

THE CHAIRMAN: Well any man who is qualified to prepare this should be qualified to express an opinion. Perhaps I should ask a question.

Q What method of depreciation is used on the books from the year 1939 until 1945. What method was used, the straight line method ?

A The straight line method, yes.

Q On how many years ?

A Ten years.

Q MR. STEER: From 1933 on ?

A Depending on the date of acquisition of the assets.

Q That is to say Royalite's books are set up on the basis of the ten year life for the original asset. The ten year life of all

part of the assets from acquisition ?

A I mean in the gasoline department. In the crude oil department the assets are depreciated a little differently.

Q If you are examining the account of any ordinary industrial undertaking, Mr. McLellan, and you are determining earnings your earnings are taken on the historical cost of the capital employed plus additions, less items discarded and less depreciation, for the purpose of ascertaining the percentage earnings of the Company. Is that right ?

A Including working capital.

Q Including working capital but my point is that in determining earnings the depreciation reserve is always deducted from the amount of the capital employed ?

A Usually.

Q That is the scientific accounting way of doing it, is it not ?

A Oh it is done other ways I understand.

Q You understand. Perhaps you will tell us about your understanding ?

A Well they are just rumours, I do not know of any specific cases.

Q Well if it is only rumour we do not need to pay any attention to rumours.

THE CHAIRMAN: We are not certain what the income tax people do.

A I do not think they determine rates of return to any extent.

Q But the deduction of depreciation from the capital value of the assets in computing your profits ?

A Well they take a portion of that capital asset. They do not deduct anything from the asset.

Q MR. STEER: Would you look for a moment at Schedule "H"

In the year 1939 I see there the balance beginning of period. I suppose that is your property account is it ?

A Yes, for that particular plant.

Q For the plant and we are talking now of gasoline plant 1. That is your total property account ?

A That is right.

Q That is the erections in 1933, additions since 1933 and items discarded ?

A That is right.

Q Then we have certain additions and deductions and then we go over to balance at end of period $377,000.00 ?

A Yes.

Q And then the balance beginning of the period. What does that mean. Does that mean your depreciation reserves ?

A Two separate classifications, assets and reserves.

Q Does that mean reserves for depreciation ?

A Reserves for depreciation at the beginning of the period. That is the beginning of 1939.

Q And you make provision for this $6,272.00 on a unit basis for the year 1939 and carry down a total of $101,000.00 ?

A Yes, that balance, beginning of period, of course is calculated on the unit method too.

Q Quite so. They are both calculated on the unit method and what I would like to get at is what that figure of $92,465.42 would be on the books of the Company and what the provision for the year 1939 would be on the books of the Company. Have you got it here ?

A No, I have not got it here.

Q You can give us that ?

A Yes.

MR. CHAMBERS: He could give it ?

MR. STEER: But you are not sure that you will.

MR. STEER: Well I am asking for it Mr. Chairman. I am going to ask you too Mr. McLellan, if you will produce the depreciation account of the Royalite Company for the years 1933 to - these figures are actually only up to 1944 are they not ?

A Yes.

Q Up to the end of 1944 ?

MR. CHAMBERS: Now sir, I am objecting to producing that, certainly at the request of my learned friend and I would frankly like to have an opportunity to argue that point before an order is made one way or the other.

THE CHAIRMAN: All right.

Q MR. STEER: Then I take you to Schedule "J", Mr. McLellan.

A Could I get that clear what you are asking in 1933 to -

Q 1944 I think.

MR. McDONALD: Before Mr. Steer leaves that point so we will know what is going to be discussed in regard to this depreciation account. Is the depreciation account of the Royalite Company covering their oil and crude operations, absorption and gas or are you sticking to the absorption plant ?

THE CHAIRMAN: I suppose we can be meticulous in our language but I think we are all talking about the absorption plant.

MR. STEER: Yes gasoline plant No. 2 and gasoline plant No. 1.

A You said gasoline plant 1 at the time.

MR. STEER: I am coming to gasoline plant 2 which is

dealt with in Schedule "J" and we have got here the balance beginning of 1939, balance end of 1939. Depreciation reserves beginning of period $63,716.74. Provision for the year $7,406.44, both of those being on a unit basis ?

A Yes sir.

Q And then carried down ?

A Yes sir.

Q And I asked you to let us have the depreciation account for the years 1933 on ?

A There was not any plant in 1933. It started in 1935.

Q Oh yes with that qualification which you might perhaps make.

MR. CHAMBERS: I take the same objection.

Q MR. STEER: While we are on that Schedule "J", Mr. McLellan, items in the first column for the years 1946 and 1947 and 1948. You spoke to my learned friend Mr. Chambers about those this morning ?

A Yes.

Q And I take it that this plant no longer is used and useful ?

A I do not know whether it is used or useful or not.

Q It was simply discarded when No. 2 plant was consolidated with No. 1 ?

A I don't know that it has been discarded.

Q What did you tell my friend Mr. Chambers about it ?

A I told him it was the equipment remaining at the location after certain of the other equipment was transferred to gasoline plant No. 1.

Q And it has been put to no use since the consolidation of the two plants. Do you know ?

A I do not know.

Q Should you not know before you make a statement like this ?

A I do not think so. As far as I know the equipment is still there.

Q But no use is being made of it so far as you know ?

A I do not know whether they are using it or not. The best of my information, it is not being used but I do not know.

Q Then we will assume it is equipment which is no longer used and useful and that being so it represents capital lost to the Royalite Company does it ?

A Not necessarily.

Q Has it got a salvage value. Did you enquire about that ?

A No I did not.

Q Whether it has any salvage value, you do not know ?

A No.

Q Whether it is capable of being used you do not know in any part of the Royalite operations. What I mean is you do not know anything about that ?

A No.

Q Well assume for the moment it was neither used nor useful and represents capital lost and you are restating these accounts for the purpose of this submission ?

A Yes.

Q Now would you look at the last page of your Exhibit 156 and what I would like to suggest to you is in making your restatements that $206,000.00 should have been written off over the length of that No. 2 plant as disclosed in the statement that you give on the last page ?

A That would be one way of looking at it.

Q And the effect of looking at it in that way would be to increase the rate of profit which the Royalite Company makes. Is that right ?

A In what year ?

Q In the years 1945 to 1948 and in the years 1939 and 1944 ?

A 1945 to 1948 it would.

Q And from the date of the consolidation of the two plants up to the end of 1944 it would do the same, is that right ?

A It might and might not. I think you would have to calculate that.

THE CHAIRMAN: Assuming every other factor in your statement remains unchanged would it not necessarily increase the profits ?

A It would increase the profits but I do not think that was what I was asked.

Q Well I thought you were ?

A I thought I was asked the rate of return.

MR. STEER: I am talking about - we only use that word rate of return with respect to a public utility generally Mr. McLellan.

MR. CHAMBERS: I think the word was used.

A I thought you were talking about rate of return.

THE CHAIRMAN: They are the same thing with the exception that one is used mostly in reference to a public utility.

MR. CHAMBERS: But the rate of return might be another thing.

Q MR. STEER: Now the effect of taking that $206,000.00 out and charging it off over the life of that undertaking would be to decrease the amount on which earnings were calculated from the time it should have been done. Am I right in that ?

A Yes.

Q And if you take the amount on which you calculate your

earnings as being $202,000.00 less than was actually used in your computations then the rate has got to be higher ?

A That might or might not be. It would depend upon what you charged to each individual year.

Q You have charged off $202,000.00 for the period 1935 to 1943. We will assume you have charged it all off ?

A Yes.

Q Before 1943 ?

A Before 1943.

Q Before the end of 1943 ?

A Right.

Q Now you compute your earnings for 1944. Is that rate not bound to be higher ?

A The rate is.

Q The rate and that means actual earnings related to the capital is higher proportionately ?

A Yes.

Q That is all that means ?

Q THE CHAIRMAN: And your operating expenses would be less by the amount of the depreciation ?

A Yes.

Q MR. STEER: I suppose we would be safe in saying, Mr. McLellan, that on the books of gasoline plant No. 1 and gasoline plant No. 2, take gasoline plant No. 1 on the books of the Royalite Company that plant would be largely written off today ?

A The No. 2 would be. The No. 1 had several new additions in the years 1940 to 1943 inclusive so that those additions would not be.

Q Those additions would not be written off ?

A Not fully.

Q Have we not got the position with regard to those additions that the Dominion Government is responsible for the payment of at least some of them ?

A I do not -

Q Is not the position under that Allied War Supply contract that some of those additions at least are going to be paid for by the Federal Government ?

A That is a matter of interpretation I think. I do not know that they are going to be paid for. We do not know. I do not think anybody knows until this contract is finally settled what the procedure is going to be.

Q But there is a possibility that the Royalite Company won't have to recover by way of depreciation some part of that capital expenditure made under the Allied War Supply contract, that is right is it not ?

A It is possible.

Q Would you look now at statement 1-A Mr. McLellan. These estimates of future years. They show a distinct drop in the sales of absorption gasoline from 1945 on. Those figures I suppose were given to you by somebody ?

A That is right.

Q And you do not know anything about the accuracy or otherwise of the estimates ?

A No. I did make a calculation by taking the number of barrels which they gave me and working that out by the product. That is the extent that I did.

Q And were they a 45 pound product or the old product before iso-butane ?

A Up to the end of 1946 they are the 45 pound product.

Q Is it said that there is going to be no demand for the 45 pound product after 1946 ?

A It is estimated by our Company that will be the case.

Q And you have not any idea of why they make that estimate ?

A No.

Q Because it does not appear to me that there is going to be a demand in Alberta, Saskatchewan and the Northwest Territories for a long time to come for high octane gasoline. You are not prepared to discuss that ?

A I am not familiar with that, no.

Q Well then if the business is going to go back to what I will call the pre-war basis. That is where you are not manufacturing this heavy product any longer ?

A Yes.

Q Should we not get the expense of operation back to the pre-war basis too ?

A Well if conditions change.

Q Have you any idea of what it is that causes the increase in operating expenses coincidentally, practically coincidentally, with the manufacture of this 45 pound product ?

A Do you mean to say in 1943 ?

Q Do expenses rise after this iso-butane product project is undertaken. Don't they rapidly.

A Of course we have only the one plant. Starting at the first of 1944 and some of our distributions of expense where sometimes we split between the two plants. Now we charge them only to one plant and the plant itself is a larger unit and so the expensesas compared with the old plant are higher due to more equipment and the necessity of employing more assistance.

Q I would have thought consolidation of the plants would probably result in less expense. You say that is not so ?

A Well it might lessen the expense as taken together. That is if you took No. 1 and 2 and added their expenses together. I do not know. I have not done that myself. As to whether it would be lesser or higher, but in this comparison you are comparing the consolidation plant with the old No. 1 plant.

Q Look at Statement No. 2, Mr. McLellan, will you. Now Statement No. 2 shows operating expenses. You first began the manufacture at least you first began to extract the iso-butane at the end of 1942, did you. Am I right in that ?

A I think so. I am not positive.

(Go to Page 5911)

Q. Well, then, your operating expense of #1 plant jumped from seventy-seven to one hundred and ten for the year 1943. Now, that would look to be applicable to the iso-butane project?

A. Yes, that would be part of it.

Q. And then it jumped for 1944 to one hundred seventy-four thousand?

A. Yes, that was when we have just the one plant now.

Q. And I am finding it a little difficult to understand why the consolidation of the two plants should result in that increase in the operation expenses?

A. Now, you take the #2 plant in 1943, the operating expense shown in Statement 3.

Q. Seventy-eight thousand?

A. Seventy-eight thousand. Now, you add that on to one hundred and ten thousand on the #1 and you have one hundred and eighty-eight thousand compared to your one hundred seventy-four.

Q. Yes. That is a fact that gives me some difficulty. I wonder, Mr. McLellan, why there should be so little saving in the consolidation, and I suppose you cannot tell me that. Then it strikes me as being worthy of comment that for 1942, as against 1943, the expenses for the latter year should be so much greater due only, as I take it, to the fact that you were manufacturing the heavy product, I should not say the heavy product, the 45 pound product.

A. I think there was a very large increase in throughput as well there. If you will notice that the revenue goes up from three hundred and ninety-five to five hundred and eighty thousand, and also the throughput, which you can find in the back here, the throughput in 1943 was 16 million M.C.F., whereas in 1942 it was 20 million M.C.F. That was a 25% increase in throughput.

Q Yes. Would you anticipate that your expense would diminsh as the throughput diminishes?

A The expense would diminish as the throughput diminishes?

Q Yes?

A Well, not in relation, but they would probably go down to some extent.

Q Because I note that your operating expenses, calculated over the years '45 to '48, do not go down very fast?

A No.

Q But your throughput goes down practically one-half, almost a half?

A No. No. Goes from 19 million in 1945 to 14 million in 1948.

Q Oh yes, I was looking at the sales. Now, would you look at the page, second from the end. Before I ask you about that, Mr. McLellan, you can probably tell me that if in the period 1933 to 1938 inclusive, making up the accounts of the Royalite Company on the ordinary industrial basis book depreciation, the percentage profit for the years '33 to '38 would be equal to or more than the percentage profit for the year 1939.

MR. CHAMBERS: I am objecting to that question, Sir. I submit that the earning, the loss or profit of this Royalite absorption plant in '33 to '38, has no bearing whatsoever in this hearing, either in fixing the absorption plant price or in fixing the well head price.

THE CHAIRMAN: Mr. Chambers, is it not a rule that when a witness makes a statement that he he can be cross-examined on it?

MR. CHAMBERS: He made no statement with regard to that. This witness made no statement with regard to the earnings of this Company prior.

THE CHAIRMAN: No, but he does show on his statement No. 1 the percentage of profit with relation to capital for the years 1939 to 1944.

MR. CHAMBERS: But there was no thought of regulation in the field at that time, and I do submit that there should be a limit laid somewhere.

MR. STEER: There is a suggestion in the record to the effect that this Gasoline Plant was built for the accommodation of the Canadian Western System. If that suggestion is withdrawn, I am not interested in the profits from '33 to '38. If the suggestion remains in the record, I submit I have a perfect right to go into the question.

THE CHAIRMAN: I think you have a right to go into the question anyway, under the ordinary rules of cross-examinatio

Q You are not prepared to tell me then, Mr.McLellan, what the percentage profits were computed in the ordinary way, in the Royalite undertaking for the years '33 to '38 inclusive?

A I do not know them.

Q You do not know them?

A No.

Q But you could find them from the books?

A It would be possible, but it is a lot of work.

Q If you had the books there in front of you in the witness box, and I asked you to make that computation, you could make that?

A Not in the witness box.

Q Not in the witness box?

A No.

Q But you could in the witness box if you had all the books and the material there, you could make that computation, couldn't you?

A Somebody would have to send food.

Q Oh sure, taking all that into consideration, Mr. McLellan, you could do it?

A I could do it here, yes.

Q I am asking you to assume that you have got the books in front of you, and that you have got the time, and I am asking you to make the computation and let me know what it is?

MR. CHAMBERS: I am advising the witness he does not have to make that computation, and I am not undertaking to have it done.

THE CHAIRMAN: Well, we will hear arguments on that later.

MR. STEER: I would say this, Mr. Chairman, that once the Board decides that we are entitled to have the information, that the simple way to do it probably would be to have Mr. Hamilton do that, the Board's accountant, if Mr. McLellan wouldn't do it.

MR. CHAMBERS: If he is given the books. But I submit that the witness in the box cannot be made to do the work, or other parties in the hearing, just because they happen to be in the box.

Q MR. STEER: Let us look at this last page then, Mr. McLellan,

A The last or second last?

Q The last. The second last, I beg your pardon. Do you know what the requirements of the Canadian Western system were for the years 1933 to 1938 inclusive?

A In respect of what?

Q Gas?

A No, I do not.

Q The evidence, I believe, is that the Canadian Western system for the years '33 to '38 inclusive, required perhaps seven or eight billion on the average a year. Seven or eight billion. Now then, we see on this statement to which I have referred that the amounts of gas processed were very largely in excess of the requirements of the Canadian Western system, that is right?

A They appear to be.

Q Am I right in thinking that, from 1939 on the lesser quantities of gas processed are due to the fact that there was a change in the policy of the Company and the amount of gas processed was accommodated to the market demand. Am I right in that?

A I do not know.

Q Yes. The figures from 1939 to 1944 show very much less gas processed on the average than they do for the period '33 to '38 inclusive. That is obvious?

A Yes.

Q And you have given us figures on a basis of unit depreciation showing substantial profits for the years 1939 to 1944, that is right?

A Showing profits.

Q 6.8%, 5.13%, 8.76%, 16.89, 12.67, 13.73; substantial profit?

A Depending on the nature of the business.

Q You think they are not substantial?

A No, I do not.

Q If you used book depreciation in computing those profits, would they be substantial?

A Well, if you use book depreciation are they profits?

Q Pardon?

A If we use book depreciation as a result of profit, that is

the question?

Q You told me a little while ago that the proper way to compute earnings was to deduct your book depreciation in finding the capital on which your earnings are estimated. You told me that?

A But provided that book depreciation is done in a scientific manner.

Q Oh sure. I would not think that a straight line depreciation over ten years, from 1933 on, for absorption plant in Turner Valley, with the knowledge that they had of Turner Valley in the past, was unscientific, would you?

A It was merely an income tax rate, I think.

Q What makes you think that?

A Just my experience in accounting.

Q From your experience as an accountant.

A My experience in auditing and their accounts.

Q Nobody in the Royalite told you that it was income tax rate, did they?

A They have not told me, but I have gathered that from my own knowledge.

Q I see. Would you have any knowledge of the Turner Valley situation as it existed in 1933?

A Would I have?

Q Yes?

A No.

Q No. And you are not prepared to say then that a 10% annual straight line depreciation rate for an absorption plant erected in that year wouldnot be scientific?

A I do not think anybody can say that any flat percentage rate at any time is scientific.

Q You say the only way that a scientific rate could be set up

would be to estimate what, the reserves in the field at that time?

A I think so.

Q Was it possible?

A Well if it is possible now I imagine it would have been possible then.

Q Now, Mr. McLellan, if your previous statement was correct, and if it is true to say that an ordinary industrial undertaking in computing earnings, as you have been computing earnings here, the computations are made on the basis of book depreciation. Now we will assume that is a true statement of fact?

A I am a little behind. You say that if these are made on book depreciation?

Q No, I do not say that. But you told me a little while ago that the proper way of making up the accounts of an ordinary industrial concern is to compute earnings?

A Yes.

Q And to deduct the book depreciation from the capital assets?

A Seeing that depreciation was calculated in a scientific manner.

Q Does it matter whether it is calculated in a scientific manner or not if it is there?

A I do not think that depreciation at any time is correct.

Q THE CHAIRMAN: But the fact is that when you provide for depreciation reserves you have recaptured some of your original investment, that is so?

A Not necessarily.

Q Then what happens to it? What happens?

A You have received certain revenues from the sale of your product?

Q Yes?

A Now, those revenues are held in the books of the Company, in the open account probably, and they may be reinvested, and there might be anything done with them, but by the time you come to the end of the period, you may have lost money. I mean, you may not get as much back as you put out. So that at any one time you cannot tell whether you have recovered your investment or not.

Q MR. STEER: Yes. Well, you won't agree? Are you recanting on that view you gave me a little while ago that the proper way was to take your depreciation and deduct it so as to find the sum on which you are going to compute your percentage?

A Provided that depreciation is calculated in a scientific way.

Q I am suggesting to you that it matters not a whit whether it is scientifically computed or otherwise, you have got the fund there.

A It may not.

Q If the fund should be invested in the capital assets, you will put it back in the proper account?

A Yes.

Q And you will have that on which to compute your earnings, and you have not done something like that here? You have got it?

A Not until you get to the end of the period, did you know that?

Q I know that. I say you have depreciation reserve in actual dollars, and until you invest it in is there in dollars, is not that right?

A You have certain things, whether they cover all the departments or not is contentious.

Q I am not interested in whether the depreciation is scientific.

I am asking you to consider this from the point of view of a Board of Directors in depreciating what they can do in the way of paying dividends?

A Yes.

Q And in order to compute their earnings scientifically, or otherwise, they have got to take it from the capital employed, and they will deduct whatever it is they have in the depreciation fund?

A Whatever depreciation there might be on the books of the Company.

Q Is there any difference in what I have said to you and what you have said?

A You said dollars on hand, and they might be reinvested in materials.

Q If it is invested it becomes part of the capital employed.

A Yes.

Q THE CHAIRMAN: And supposing there are distributed in capital repayments to the shareholders, what then?

A They are no longer in the business, then.

Q No.

Q MR. STEER: I am going to ask you to assume that I am right, and to assume that the proper view for a Board of Directors to take is what I have suggested to you, that they are going to deduct the book depreciation from the capital employed for the purpose of determining their earnings and dividend policies.

A Yes.

Q That is clear, isn't it?

A Yes.

Q Now then, with regard to this statement 1, if we look at it from that point of view, you know enough about

the depreciation account of this Royalite Company, to know that that 6.8, 5.3 and 8.7 would be very much larger percentages computed in the way I have suggested?

A Yes, they would.

Q And you know also for the years 1933 to 1938 you would have similar percentages or higher, having in mind the much larger volumes that were processed over those periods. Now, my friend, Mr. Chambers, wants to say something, I think.

MR. CHAMBERS: I object to that being gone into.

THE CHAIRMAN: Why did you take 1939 as a starting point, Mr. Chambers?

MR. CHAMBERS: Because some people wanted some information. I still do not think that it is relevant, but I do not want to be technical and I do not want to be accused of trying to withhold some information of some value. First of all, Mr. Hamilton went into 1943, and I say that he should have taken more than one year, the years prior and the years following, because we think it would give a better picture. They want to go back to 1933 now, and I do submit that they should not be permitted.

THE CHAIRMAN: Supposing I come to make my allocation, Mr. Chambers, and I look at 1939 and I see there that there is so many cubic feet and on that amount you made 6.80% as shown in Statement 1, and I go back to 1933 and I find that you processed two and a half times what you did in 1939. In the absence of evidence, am I not justified in saying, that your rates then would be two and a half times the other. I do not say that I would do that, Mr.Chambers, but might I not be justified in doing that in the absence of evidence?

MR. CHAMBERS: I submit that if you are going to

assume that that you would have to assume some other things.

THE CHAIRMAN: Quite right, Mr. Chambers. I agree with you, but something of that kind could happen.

MR. CHAMBERS: Now, Sir, if I might say it again, and I am sincere about this, I do not want to object to questions for the sake of withholding information, but I do submit that there has got to be some practical limit and, rightly or wrongly , I do submit that Section 72(4) restricts the extent to which my clients' books can be examined. I do not want to avail myself of it, and I want to bring out any reasonable information, but I do submit that subsection 4 of Section 72 makes it clear that it is not a public utility hearing so far as the absorption plant earnings are concerned. Subsection 4 of 72, as you recall, deals with this matter, and it says;

> " For the purpose of carrying out the provisions of this section, the Board in addition to any other powers conferred by this Act or any other Act, shall have the power to require and compel the attendance of the proprietor or any officer, agent or servant of the proprietor of any absorption plant, and to compel the production of documents related in any manner to the operation of any such plant and with regard to the attendance of such persons".

and so on.

Now, I submit that the operation of the plant certainly under that section, does not refer to the earnings of this Company, either of capital or in the capital charges back to the 1933, eleven years before the Act was passed.

THE CHAIRMAN: Would you suggest Mr.Chambers, that I make my allocation on estimates for the future rather

than on the figures of the past?

MR. CHAMBERS: I think and I submit that the Board has no authority under the Act to try what was done in the past. Now, that is my position. It must be done as from 1944, and that the minute you are going back to take the why and the wherefore of the period from 1933 to 1944, you are sitting in judgment on that.

THE CHAIRMAN: You know that the Legislature is still in session, Mr. Chambers.

(Go to page 5923)

Q What are you prepared to tell us Mr. McLellan about the profits from 1933 to 1938 compared with the profits on the average ?

MR. CHAMBERS: I instruct you not to answer until the Chairman directs you to answer.

THE CHAIRMAN: We will leave it for today, Mr. Steer.

MR. STEER: Yes sir.

Q Would you look at Page 5, Mr. McLellan, of the report ?

A Statement 5 ?

Q No, Page 5.

A I am sorry.

Q I have got to come back to this question of the allocation of cost as between gasoline and the natural gas departments. Those figures that you have given us there and the percentages I take it are the percentages of the actual volume of gas that went into the absorption plant that was used up in the process of the absorption plant, is that right ?

A I say I think so. I say that because these figures were given to me from the field, Turner Valley.

Q As what were they given to you ?

A As the basis upon which I should distribute the gathering and compressing costs. The volumetric basis.

Q Then are we to take it that in the case of the year 1939 we will say that 4.99 was 5% ?

A Yes.

Q That 95% of the gas that went into the absorption plant went out through the residue outlet. Are we to take that ?

A I do not think I should say because I did not make these figures up.

Q I wonder if you will find out for us and let us know ?

MR. CHAMBERS: Yes, we will do that.

MR. STEER: Excuse me just a moment.

Q Now I am not sure Mr. McLellan whether I exhausted this subject with you or not, but suppose I ask you this would you be able to give me an answer. What percentage on the labour basis of the indirect charges has been charged to each department, namely crude oil, gasoline and gas ?

A The indirect charges were not charged on the labour basis.

Q Yes. What you told me is that you did not have the departmental books at all ?

A Yes.

Q But you had what did you call them, plant books ?

A Unit and main classifications.

Q Units, and you can go to each one of those unit books and could pick out the direct labour involved in that unit ?

A That is right.

Q And then tell us what you did after that ?

A Firstly we take all our direct labour in each of those units.

Q Yes ?

A Then we take our welfare and administrative and general and distribute those on a labour basis to each individual unit.

Q Oh yes ?

A Then that increases, sometimes decreases the expenses of the service units.

Q Yes ?

A Now that service unit in the first place was charged out to various other units on sometimes a percentage basis and sometimes - well there are lots of bases that they are charged out on. So that we then charge this new expense which we have in the service unit, that is welfare and administrative and

general expense out on the same basis as it was originally charged, as the other expenses in these units were originally charged.

Q Taking the three departments as 100% of the direct labour what percentage does gas, gasoline and crude oil compare to each of that 100%. Can you tell us that ?

A No, I cannot.

Q Could you ?

A I think it would be pretty difficult because for instance I take some of my labour and put it into my storehouse. Now some administrative expense, for instance welfare expense is attributable to this labour and I charge it to expense of my storehouse. Now the storehouse overhead is charged out on a percentage basis to each individual issue. Well there may be three hundred or four hundred issues in a month and they go all over the accounts, to every little sub-classification, so it would be almost an impossible task.

Q Then it comes to this, that you are not able to tell us, either on a percentage or a dollar amount the charges for labour, direct or indirect, against any one of these departments ?

A That is right.

Q That is right ?

A That is right.

Q And there is no way of getting it from your books ?

A I do not think so.

Q That is all, thanks.

CROSS-EXAMINATION OF THE SAME WITNESS BY MR. HARVIE:

Q Mr. McLellan on Page 6 of Exhibit 156 that we have been referring to, under the paragraph dealing with revenues ?

A Yes.

Q I think Mr. Steer in part brought out the point that I just wanted some further elaboration on. I do not know that he did it entirely. Where it is said in that paragraph "It is assumed that the present product will not be manufactured after the end of 1946." I think you told Mr. Steer that you meant by that there would be some other product than the 45 pound ?

A Yes, that is right.

Q Was there any specific product that you had in mind do you know ?

A No, I do not know. As I say these estimates were given to me by the engineer.

Q "If such is the case, the number of barrels which are recovered from a certain amount of gas will be less than in the years 1945 and 1946". Can you give us any further information on that ?

A Well we recover a certain number of barrels per Mcf from the gas which we process under the 45 pound product. If we make a lighter product we recover - well I am not sure whether it is lighter or heavier to tell you the truth.

Q It varies with the type of product ?

A That is right. The recovery varies with the type of product.

Q Were there any specific figures used in these estimates do you know ?

A Yes.

Q On what basis were those - -

A So many barrels per thousand Mcf.

Q That means so many barrels if it had been the 45 pound product ?

A No we took the actual throughput and assumed that we would recover so many barrels per thousand Mcf.

Q Then in 1947 to 1948 what percentage of production did you take?

A I have not got the figures right here Mr. Harvie.

Q Do you know whether that was on the basis of going back to the 26 pound product ?

A No, I don't.

Q Where you deal with the revenues do you know what figures you used as to the value of the product ?

A Yes, $1.90 a barrel.

Q For 47 and 48 ?

A For all of it.

Q All the way through ?

A Yes.

Q Whether they are 46 or 26 ?

A That is right.

Q Now share to the producer, the next paragraph. You state I think "This has been estimated at 20% of the estimated revenues, with the exception of the year 1945, where the figures represent the actual amount of the payments made to the producer." Why would there be any difference in 1945 over the estimate of 20%?

A In 1945 the percentage is calculated on the actual production of the plant whereas in the estimated years it is calculated at 20% on the sales, assuming all production will be sold.

Q That is all, thank you.

THE CHAIRMAN: Mr. McDonald ?

CROSS-EXAMINATION OF THE SAME WITNESS BY MR. McDONALD:

Q Would you just refer to Schedule "J" Mr. McLellan and come to the figure 1948, or 1946, balance at the end of the period $205,827.76. Will you tell me how much of that figure comprises fixed assets such as real estate, buildings, cement foundations and immovables ?

A No, I cannot.

Q It does comprise something of that kind ?

A Yes.

Q Have you any idea how much comprises movable machinery, pipe that can be taken up ?

A No, I have no idea as to the content of that.

Q You can get that figure for me can you not. Can you break that down ?

A Yes, that can be broekn down.

Q What I have in mind Mr. McLellan is that obviously the materials that cannot be moved and not used elsewhere, unless that plant is opened up again is irretrievably lost as far as the absorption plant operation is concerned. I want you to have that in mind when you make up your statement. Can you tell me this, your refractionator, referred to along with gasoline plant No. 2, has that been moved to plant No. 1 ?

A Not as far as I know.

Q The Schedule "M". This is compressor station No. 2. In what part of the field - -

A Not Schedule "M", "N" I guess it is.

Q Yes, "N". In what part of the field is compressor station No. 2 situated ?

A In the south end.

Q Is that amalgamated with this No. 3 plant ?

A I do not know.

Q I notice that in 1946 the investment remains static to 1948 ?

A Yes.

Q And the same comment applies to this investment as to the compressor station ?

A The No. 2 plant ?

Q Yes, the No. 2 plant I mean. Would you let me have a detail of that investment as between real estate, foundations, immovables and machinery that is movable and has a prospect of future life, future use ?

A Yes.

Q With regard to Schedule 4, where did you obtain your basis for salvage with regard to - -

A I got that from the engineers in the field.

Q You do not know what considerations they took into account ?

A No, they just gave me the figures, in detail of course.

Q Now will you tell me with regard to this payment to Royalite under the Allied War Supply contract ?

A Yes.

Q As I understood your evidence Royalite received $95,400.00 on December 18th, 1943 and $13,595.12 on April 17th, 1945 ?

A Yes.

Q A total of $108,995.12 which I understand was invested in materials or invested in assets that now comprise part of your absorption plant ?

A No, that money was received by the Royalite Oil Company.

Q Was it received on account of assets that now comprise part of the absorption plant ?

A No, it was received under a contract with the Allied War Supplies Corporation.

Q What I am trying to get at is, is that figure that you have picked out there applicable to the absorption plant business of the Royalite Company ?

(Go to Page 5931)

A It is applicable to the installation of certain additional equipment at the #2 plant, and the moving of the #2 plant to the #1 plant, and consolidation in the #1 plant.

Q Under the terms of the contract, final settlement may result in the Royalite Company repaying to the Crown some part of that money?

A Some or all.

Q MR. STEER: Or getting more money?

A Yes.

Q MR. McDONALD: So that when that matter is finally adjusted, will there be any revision in the figure you have submitted in your Exhibit 156 as regards the capital investment ?

A I do not think so.

Q THE CHAIRMAN: Why not?

A Well firstly, we have a plant here which is being used by certain people, and in calculating a statement of this nature the producer was primarily interested in this calculation, and it is contended that the total value of the plant, regardless of where it came from, should be charged to the producer in any operation, that is he should pay for the value of the plant.

Q And the other is just a pleasant bonus from the Dominion Government?

A I do not know, sir. Assuming that the shareholders put some money up.

THE CHAIRMAN: I think it would be the depreciation reserve would put most of it up, not the shareholders.

Q MR. McDONALD: Just on that point, Mr. McLellan, if you will look at Statement 2. The second last item. "Less costs of moving gasoline plant #2 to gasoline plant #1,

1943, $5,794.34, and $39,289.50 in 1944."

A Yes.

Q Now was some of the $108,000.00 odd actually used in meeting that expense that is charged there?

A No.

Q That is over and above anything that was allocated from that fund?

A That is right.

Q Dealing with that statement too, Mr. McLellan, you say in the last item "Profits, Gasoline Plsnt #1". That was out of the compensation scheme settlement?

A Yes.

Q $96,696.59?

A Yes.

Q Now the balance of the compensation, roughly $100,000.00, is that expense charged against the dry gas market?

A Yes.

Q Against the dry gas sales?

A And a little against the crude oil department.

Q A little against crude oil?

A Yes.

Q Now turning to page 5, Mr. McLellan, on the allocation of the gas gathering and compressing costs. Can you tell us how the balance of the gas gathering and compressing costs in 1939, roughly 95%, were charged? Were they charged against the gas market?

A I did not complete my statement to that extent. All I was concerned with was the gasoline plant. I assume that is where it would be charged.

Q It might have been charged to Boiler Plant, Electric Plant and things of that kind?

A No, no. Just 5% to the Gasoline Plant Department, and 95% to the Gas Department.

Q Now then, if say 50% of the gas gathering and compressing costs were charged against the absorption plant, you would have a very much different statement from 1939 to 1944?

A Yes, I would.

Q Yes, and as I take it your calculation from 1939 to 1944 was on the volumetric basis, and that is what you continued on in the future, 1945 to 1948?

A That is right. Those figures I did not calculate myself, They were calculated in Madison statement M-9.

Q In the 1945 to 1948 you used the M-9 figures?

A Yes.

MR. BLANCHARD: And 1944, I suppose you used the 5% figure?

A Yes, that was the actual charge for 1944.

Q MR. McDONALD: In 1944 you used the actual amount that the Madison charged to the Royalite Company?

A That was 5%.

Q Of the absorption gasoline sales?

A Yes.

Q So that if there is to be an allocation of costs, other than the basis on which you have set out in this statement, all your calculations would have to be revised?

A Oh yes.

Q As to profits and losses in the future?

A That is right.

Q And the rate of return?

A Yes.

Q Did I understand Mr. McLellan, in your answer to Mr. Harvie that you used a flat rate per barrel of absorption products

Q Now just one other item, Mr. McLellan, in your estimates or in your calculations from 1939 to 1944, you have estimated the income taxes to be used in your operating expenses?

A Yes.

Q And the reason for that was because the method of depreciation was different from what you actually used?

A That is right.

Q MR. HARVIE: I do not like to interrupt you there, Mr. McLellan, but in connection with your reply which I gathered to Mr. McDonald's question about the four or five pound product, would be more valuable than the six pound product.....

A No, it was in the past, has been in the past.

Q But at the present time?

A I do not know what it is now.

MR. HARVIE: I asked that because I did not understand it.

MR. McDONALD: And that is all.

MR.CHAMBERS: I wonder if we might adjourn now? Mr. McLellan has been in the box since 10 o'clock this morning and there is a matter that he and I would like to discuss perhaps with Mr.Brownie.

THE COURT: All right.

MR. CHAMBERS: And I had in mind we could probably finish with Mr. McLellan tomorrow and if it meets with the convenience of Counsel, I would like to put Mr. Smith in tomorrow, and I suggest we have him ready the first thing in the morning, on the question of actual operating expenses, throughput and so on, of Madison for 1945. That is something which should go on the record anyway.

THE CHAIRMAN: All right. We will adjourn then until 9.30 tomorrow.

(The Inquiry was here adjourned, to be resumed at 9.30 A.M. March 13th, 1946).